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THE CLASSIFICATION OF PUBLIC REVENUES.

Two years ago, in the *Quarterly Journal of Economics* for April, 1893, an attempt was made to throw some light on the classification of public revenues. In all the main points I still hold to the views therein expressed. So in especial to the classification into gratuitous, contractual and compulsory revenues; the division of the last class into special assessments, fees and taxes; and the discussion of the relation of the taxing power to the police power of the state. But in one point further reflection has induced me to modify my view. And, since truth is more important than the consistency of any individual, I take this opportunity of stating what I now consider to be the correct view.

The point is this. Where shall we class the payments made for certain governmental enterprises like the post-office, railroads, water-supply, etc.? In the original article it was maintained that these payments fall into different categories, chiefly according to the conditions attending the enterprise; and the conclusion was drawn that the payment for the same service may be a price in one state, a fee in a second, or a tax in a third. I am now convinced that, while the conclusion is perfectly correct, the reasons given for the conclusion are partly invalid, and that the explanation is to be sought in an elaboration of the very principle which was employed to show the difference between special assessments, fees and taxes. In other words, the controlling consideration in the classification of public revenues is not so much the conditions attending the action of government as the economic relations existing between the individual and the government.

Let me attempt to make this clear by taking up in turn the various classes of revenue.

The simplest case arises when the government decides to go into a purely private business. The government sees private individuals making money out of certain occupations, and asks itself why it also should not do the same. It therefore enters upon the business, and conducts it in precisely the same way as an individual would do. Instances of this were very common in former times, when governments carried on all kinds of private occupations, such as manufacturing pottery or loaning out moneys or conducting various commercial enterprises. In modern times this has become less usual. But many states still own real estate, either renting it out or utilizing it and selling the produce in the open market; some states still carry on a banking business; and others deal in commodities, like Holland in tobacco, Chili in guano, and India in opium. In all such cases the chief consideration with the government is fiscal. The charges are precisely the same as would be made by private individuals. In fixing the price, the government is actuated by the same motives that obtain in private business, whether the business be competitive or monopolistic. It is immaterial to the purchaser whether he buys from the state or from a private person. He has to pay the same in each case. The commodity or service supplies his own private wants, and there is nothing public about the transaction except the mere accident that the seller is a public agent rather than a private party. In such a case as this, then, the business is an essentially private business; and the charge made by the government is a quasi-private price. It is a purely contractual payment, resting on an agreement between the government and the purchaser. The special benefit which the individual receives is the controlling consideration to him. The matter of general interest or of public purpose is only an incidental matter.

We now come to the next case where the government

decides, for special reasons which are not purely fiscal in character, to enter upon certain more or less industrial enterprises. It is found by experience that the retention of these enterprises in unregulated private hands is not thoroughly satisfactory. The government indeed may decide to leave these occupations to private initiative; but it then attempts to regulate the business very energetically. Or it may prefer to take over the business into its own hands. The reason for interference is that of public policy. It becomes a matter of common interest, not purely and solely of private interest.

The familiar examples of such enterprises are the post-office, the telegraph, the telephone, the railway, the water, gas, and electric-light supply. These are often called economic or natural monopolies, because through the working of economic forces competition in these enterprises tends to become inoperative. In most cases, too, they can be carried on only in virtue of some privileges or franchises conferred by the government. The public interest is therefore admittedly a strong one: whether it take the shape of governmental regulation or of governmental ownership is, for our special purpose, immaterial.

Let us assume the latter to be the case. The problem then arises, What is the nature of the charge made by the government for the service, or the commodity which results from the operation of these enterprises?

The chief point is still the private interest of the individual. He buys his gas or his telegraph service to satisfy his private wants, very much as he would buy it from any individual or corporation. But a new element has entered,—the public element, the satisfaction of these wants which one feels as a member of the community. The very reason that these enterprises have been made government enterprises is precisely because the individuals who compose the community feel that they have a common, public interest in the assumption of the business by

the government. They believe in municipal water-supply, for instance, because they are convinced for various reasons that this business ought not to be left in private hands. The government, indeed, may make a charge; and this charge is undoubtedly a price paid by the individual. But it differs from the private prices. In the one case — the case of the private business — the monopoly looks only at greatest possible profits. In the other case — that of public monopoly — the government looks at the greatest possible public utility. It is true that the government may conduct this business in various ways. But, even when it makes a high charge, this charge is not fixed simply by the idea of maximum monopoly profits. The public element always comes in to modify the charges in some particular. If it did not, there would be no reason for the assumption of the business by the public.

The charge to the individual is thus a price, but, instead of being a quasi-private price, it is now a public price. The relation of the government to the individual is not the same as in the preceding case. The special benefit to the individual is less than before, although it is still preponderant. The public purpose has become of more importance.

But — and now we come to the really important point — the feelings of the citizens may undergo a change, and may induce the government to manage the enterprise in a different way. The element of private individual interest or special benefit may diminish, and the feeling of public interest may increase so as to become the controlling consideration. The government, because of these changed conditions, will now decide no longer to run the business on the principle of profits. It will reduce the charges somewhat, so as perhaps only to cover the cost of operation, or not even to cover this cost. And, while it will still roughly endeavor to charge each individual according to the benefit he derives, it will still further

modify these charges in the direction of the public interest, charging less to those who can afford it less. In other words, special benefit to the individual is still measurable and charged for; but, since the common interest of the community is now of more importance, the special benefit may be slightly modified by other considerations, as in the case of the postal service, where newspapers are put in a lower class than letters. The charge to the individual has now become a fee.

Finally, another change may occur. The citizens may become convinced that the public purpose has become the exclusive consideration, and that the special interest of the individual is swallowed up in the general interest. The government will now entirely abandon the principle of charging according to special benefit, and will do one of two things. It will either make no charge at all to the individual for the special service, or, if it still makes a slight charge, it will charge not according to the principle of special benefits, but primarily according to the principle of faculty or ability to pay. The expenditure must indeed be defrayed, but it will now be defrayed by a general charge on the whole community, or a charge upon that section of the community which avails itself of the service; but even here it will not measure the special charge to the individual by the benefits he may individually receive. In other words, the payment is now a tax; in some cases a general tax, in other cases a special tax.

Let us illustrate this process. A railway is in private hands, and the individual traveller or shipper pays a private price. Now the government buys up the railways. If it manages them in precisely the same way, the payment made by the individual would still be a price,—a quasi-private price, because made by the government acting as if it were a private party. But the government is likely soon to introduce some changes in the public interest, although it still seeks to make a profit. Because

of the changed relations between the enterprise and the patron, the payment is now a public price. After a short time the government may reduce its charges considerably, barely covering the cost, and may modify them still further by considerations of public policy in regard to individuals or to sections of the country. The payment is then practically a fee or toll. Finally, the demand may be made in the public interest, as in Australia to-day, for free railway travel. The payment made by the community to defray the gratuitous railway service would then be a tax. In the case of the common highways and the canals, this same evolution is discernible; and the final stage of free travel has actually been reached.

Take the water-supply as another illustration. At first it is often in the hands of a private company. Then it may be managed by the city, but according to the same principles. Every one pays in accordance with his consumption, but he pays more than it costs the city to supply the water. The enterprise is managed on the principle of profits. Then comes a change. The city still charges according to consumption, but charges only cost. Then often comes another change; and the city, while still trying to make both ends meet, charges each individual a lump sum, but makes the richer consumer pay more than the poorer consumer, even though he consumes no more. Finally, we reach the stage already attained in some European cities, and now demanded for Detroit by Mayor Pingree, where the water is supplied to the citizens without charge, and where the expense of water-supply is put in the same category as the expense of street cleaning. The charge for water-supply has thus run through the various stages—private price, quasi-private price, public price, fee and tax. Some cities, indeed, may have jumped over the intermediate stages, may have started with the final stage, or may never have reached this stage. In fact, although this is unusual, the prin-

ciple of development itself may be reversed, the public interest may lag, and the principles of private management may again be introduced. But the principle itself is everywhere discernible, whether it works forward, as it usually does, or backward, as in some exceptional cases.

What has been said of the railway and water-supply may be repeated of all other governmental enterprises — the highway, the canal, the post-office, the telegraph, the telephone, the gas and electric light, the street railway and trolley line, the management of the docks, the markets, and the ferries. And, if the socialistic scheme is ever introduced, the same principle would apply to all the cases of governmental management of what had once been private enterprise. I am, of course, not discussing whether the government ought to assume these enterprises. I am simply elucidating the economic and fiscal nature of the payments made, or to be made, by the citizens.

The demands made by government for supplying the individual with commodities or services differ in character, then, according to the economic relations between the government and the individual. It remains true, as was stated in the preceding article, that just as a fee may become a tax, so it may become a price and *vice-versâ*; and it also remains true that, while a price can never be a tax, the payment for the same service may take the form of a price in one state, a fee in a second, and a tax in a third. But the criterion is not, as was originally stated, the fact of monopoly or competition. The real test is the economic relation between the individual and the government, and the relative strength of the individual private interest as compared with the common, public interest.

While there is thus a clear distinction, chiefly of degree indeed, between a price and a fee, and a fee and a tax, we find in actual life some payments which combine separate elements, and which it is difficult for any one but a trained

observer to detect in their real relation. Take, for instance, the combination of price and tax. If the liquor business is in private hands and the government imposes a tax on each glass sold, the individual pays a certain amount which includes both price and tax. If the price of a glass of liquor is five cents and the government levies a tax of one cent, the individual pays six cents, of which five is the price, and one is the tax. Now, when the government has a monopoly of the liquor manufacture or trade, as in some countries, the relation is exactly the same. The government may charge more than six cents. In fact, that is generally the reason why it introduces the monopoly; but it is only the surplus over five cents that is the real tax. The same is true of other fiscal monopolies, like the tobacco or sugar or salt monopoly. What the individual pays over and above what we would have to pay to a private vender is the indirect tax. The same might be true of the railway, or water-supply, etc. But this scarcely ever happens at present, because the railway and water supplies are not fiscal monopolies. They may be monopolized by the government; but in almost every case the object is not to raise the price, but to diminish the price, not to make profits, but to secure general social utility. Yet, just as the French government imposes a tax on the private railway tickets, which is added to the price of the tickets, thus distinguishing between the price and the tax, so the same thing might be done if the railways were owned by the government. The payments would be economically distinguishable.

In the same way the identical payment may include a fee and a tax, as was abundantly illustrated in the preceding essay. Governments do not usually make the sharp distinction. For instance, some American states speak of insurance fees; and other states call the precisely identical payment insurance taxes. So the agricultural fees in some of the Southern states are some-

times called fertilizer taxes; and on the continent the terms "fees" and "taxes" are often indiscriminately applied. Practically, it may not be of great importance in all cases. But in theory the distinction is clear, and it is beginning to be recognized in our courts.

A more difficult and confusing case arises when one payment is levied in the form of another payment. The most familiar case is that of a public price levied in the shape of a tax. Take the water or gas supply for instance. In Europe, when the towns bought out the private water or gas companies, they at first continued to charge on the same principle, according to individual consumption. Some of them do so yet. But in some cases, for purposes of convenience, they assumed that each household would consume a certain quantity. And, as some of the local taxes are levied on the occupier, they simply added a certain amount to the tax. So, for instance, in some English towns where a special water rate is levied like the other local rates, or in Austria where an addition is made to the local tax on house rent. But the payment is nevertheless a price, and not a tax; for if more than the assumed normal quantity is used by any one, especially a business man or factory owner, the charges are increased according to the consumption. If the charges were reduced, or if all idea of special benefit were abandoned and the charge were assessed on the whole community or part of the community irrespective of the relative quantities consumed by any one, then the payment might become a fee or even a tax, whether general or special. But, as a matter of fact, in most places to-day the payment is still a price, even though sometimes levied in the shape of a tax. Thus in England there is a separate class of municipal revenues called income from "gas and water undertakings," which proves that they dimly recognize the distinction. And in New York the charge for Croton water is technically called

the "water rate" or "water rent," although most people call it the water tax, and confound it with a tax. In New York, it is true, this "rate" is paid separately; but in some of the European cities, for purposes of convenience, it is simply tacked on to some existing tax. But as long as the economic relation of the individual to the government is a different one, so the charges, even though confused in the same appellation, are really different.*

We may thus explain the classification of public revenues, in so far as the classification is of actual importance to-day, in two ways. If we divide them into contractual and compulsory revenues, there is no doubt that we must put quasi-private prices under the former head, and fees, special assessments, and taxes under the second head. But the public prices, the charges made for industrial enterprises under certain conditions, occupy a middle position, and might be called semi-compulsory. If the government manages the enterprise just like an individual, then it is virtually a contractual payment. If the government makes the whole community or part of the community pay, it is a compulsory payment. But, if the government employs the intermediate principle of charge, then the payment is neither wholly contractual nor wholly compulsory, but contains elements of each. The classification would then be as follows:—

Revenues.	{	Gratuitous . . .		Gifts
		Contractual . . .	Public Property and Industry	Quasi-private Prices.
		Semi-compulsory . . .	Public Property and Industry	Public Prices
	{	Compulsory . . .	Eminent Domain	Expropriation.
			Penal Power	Fines and Penalties
			Taxing Power	{ Special Assessments. Fees Taxes.

* The statement in my original article that the English water rate is a special tax is an error due to the confusion just mentioned. Further study has shown me that the charges made by the English towns for water are exceedingly diverse, and rest on very different principles in the various towns, but that they are almost everywhere still "public prices." What they will become in the near future is uncertain.

But if the real distinction is, as we have suggested, the economic relation of the individual to the government, the classification of the charges would depend upon the importance of the individual interest measured by the special benefit to the individual, as compared with the common interest or public purpose, measured by the ability of the individual to contribute to public charges. In the one case the individual is the chief or only factor: in the other case the individual sinks his own importance in the common welfare of the community, and whatever benefits he derives come to him only incidentally as a result of his membership in the community. As at one extreme lies the price, which holds in mind the relation of government to some particular industry or individual, at the other extreme lies the tax which holds in mind the relation of government to all industries or individuals. Midway between these extremes lie the special assessments and fees, whose characteristics were fully elucidated in the original article. We might thus classify as follows, omitting as of no importance the titles of expropriation and fines:—

1 Special benefit, the exclusive consideration	Public purpose incidental	Quasi-private Price.
2. Less special benefit, although still preponderant.	Public purpose of some importance	Public Price.
3 Special benefit assumed	Public purpose absolutely necessary	Special Assessment.
4. Special benefits still measurable	Public purpose the controlling consideration	Fee.
5 Special benefits only an incidental result.	Public purpose the exclusive consideration, principle of faculty or ability	Tax

The above classification would result in the following definitions:—

A *quasi-private price* is a voluntary payment made by an individual for a service or commodity sold by the government in the same way as a private individual would sell.

A *public price* is a payment made by an individual for

a service or commodity sold by the government primarily for the special benefit of the individual, but secondarily in the interest of the community.

A special assessment is a payment made once and for all to defray the cost of a specific improvement to property undertaken in the public interest, and levied by the government in proportion to the assumed special benefit accruing to the property owner.

A fee is a payment to defray the cost of each recurring service undertaken by the government primarily in the public interest, but conferring a measurable special advantage on the fee-payer.

A tax is a compulsory contribution from the person to the government to defray the expenses incurred in the common interest of all, without reference to special benefits conferred.

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